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SUBJECT: RUSSIAN MIDDLE CLASS NOT DEAD YET?

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Classified By: EconMinCouns Eric T. Schultz, Reasons 1.4 (b,d)

SUMMARY

¶1. (C) Leading Russian sociologists concur the GOR missed the chance to invest in the middle class during the economic boom. As a result, the middle class remains only approximately 20 percent of the population. That said, experts assert that the small middle class is nonetheless well positioned to weather the current crisis owing to its savings and human capital. Moreover, they see the middle class less as a revolutionary class than an inert mass, inclined to support the administration. Neither sociologists nor the administration consider the middle class a threat to the regime, even in the throes of an economic downturn. As such, the government has decided to focus its anti-crisis resources on blue-collar workers instead of providing the support and institutional reform needed for middle class development -- and ultimately the innovation economy that Medvedev and Putin advocate. End Summary.

MIDDLE CLASS SURVIVING, BUT NOT THRIVING

¶2. (U) During last month's annual conference on the sociopolitical challenges of the 21st century, sponsored by the Independent Institute for Social Politics (ISP), panels of sociologists and economists, many of whom advise President Medvedev, said the Russian middle class would survive the economic crisis but would not thrive. Igor Yurgens, of the Institute for Modern Development, opened the conference by underscoring the GOR's neglect of investment in the public and social institutions necessary to nurture the middle class during the eight year economic boom that coincided with Prime Minister Putin's presidency. The opportunities provided by massive petrodollar inflows were now gone, he stated. Owing to the government's failure to capitalize on these opportunities and the reversal in Russia's economic fortunes, the vertical impetus for social mobility had stopped functioning.

¶3. (C) XXXXXXXXXXXX, further stressed the lack of quantitative middle class growth in spite of Russia's economic prosperity. She used studies from 2000 and 2007 to demonstrate that the size of the middle class remained relatively constant, at anywhere from 12 to 20 percent of the population. By her estimate, the core of the middle class was between 5-7 percent of the population, although by lowering the income standards and the standard

set for social and professional status, the middle class would then range between 12-20 percent of the population. In her calculations, the middle class was made up primarily of managers of large companies, bank directors, financial specialists, business owners (restaurants, retail trade), part of the intelligentsia, and middle to high-level bureaucrats. The latter category had grown during the crisis (owing to the slowdown in the private sector), and she said, now comprised about a quarter of the middle class.

GETTING THROUGH THE CRISIS

14. (C) During a separate meeting with us, XXXXXXXXXXXX claimed that the fall in real incomes, not job losses, was now the biggest threat to middle class prosperity. XXXXXXXXXXXX estimated that middle class incomes would shrink this year by 10 to 15 percent with a negative GDP growth rate of 3.5 percent. (In comparison middle class incomes dropped by 25 percent during the 1998 crisis). She added that the "core" of the middle class had actually contracted slightly, from 6.9 to 5.3 percent, which she said was probably due to the fact that a number of white collar workers (bankers, managers, as well as small and medium sized entrepreneurs) had fallen out of the middle class since the beginning of the crisis. She contended, however, that the employment situation with the middle class had for the most part stabilized.

15. (C) XXXXXXXXXXXX commented that the middle class had certain "cushions" which gave it an advantage over the blue collar, or poorer classes during the crisis. First of all, many of the middle class had accumulated

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savings during the boom years (comprising between seven to 10 percent of their total incomes, or the equivalent of four or five monthly salaries). Between October 2008 and February 2009, they tended to take advantage of the GOR's gradual devaluation to purchase foreign exchange, trade it for rubles, and then purchase large consumer items and durables, such as automobiles and refrigerators, which were priced in rubles. She said as of February, however, the middle class "consumer binge" had pretty much run its course owing to the decline in real incomes, depletion of personal savings, and persistent inflation.

NOT REVOLUTIONARY

16. (C) Despite claims by political activists like Garry Kasparov that the middle class will create "problems" for the administration when job cuts start and salaries freeze, most sociologists here portray the middle class as a conservative force rather than a potentially disgruntled constituency eager to defend its interests. XXXXXXXXXXXX argued the number of "entrepreneurs" within the middle class had not grown during the Putin years. He claimed virtually all of the growth had come instead from the rise of government bureaucrats who benefited from impressive pay increases under Putin. As a result, the mentality of the middle class has shifted considerably away from the more independent and market-oriented conceptions of the Yeltsin-era (in which entrepreneurial types dominated).

17. (C) During the Putin era, Russia has developed what XXXXXXXXXXXX termed a "third world" middle class with a conservative mentality, shaped by hierarchical thinking, and largely risk averse. Indeed, according to his research, the core of the middle class has now absorbed much of the bureaucratic worldview of the majority. This explains the broad support for Putin and Medvedev across society, the power of social conservative values, and a reluctance to challenge authority.

18. (C) Paradoxically, Russia's youthful middle class is more

Western in its lifestyle, but still very anti-Western in its politics, according to XXXXXXXXXXXX. She sees Russia's young "social innovators" (her company eschews the term "middle class" as too controversial) as characterized by a more Western lifestyle, including the willingness to take bank loans, use the internet, pay for fitness centers, etc. Their better education makes them mentally more flexible but does not make them more politically liberal. Far from afraid of the economic downturn, most are confident that their abilities allow them to re-invent themselves and adapt to challenges.

¶9. (C) XXXXXXXXXXXX commented to us that today's youth are firmly indoctrinated in a "patriotic" mindset that blames the US and the West for much of Russia's ills. They remain largely apolitical, but more attuned to the interests of the state, rather than the rights and opportunities of the individual. As such, he sees Russia's youth as more inclined to rally in defense of the state than to agitate for revolutionary change.

MIDDLE CLASS WELL POSITIONED, BUT LACKS SUPPORT

¶10. (C) That said, XXXXXXXXXXXX and XXXXXXXXXXXX told us in separate meetings that the middle class still had the best chance of stimulating Russia's development in the post-crisis world. It had invested more in its own human capital (education and training) during the high growth years; whereas the lower socio-economic strata used most of their new-found cash to purchase basic consumer items. In addition, the middle class had acquired work experience and professional skills enabling them to adapt to shifts in labor market demand. Blue-collar households, in contrast, were suffering disproportionately from inflation, down-sizing, and salary reductions. XXXXXXXXXXXX concluded the middle class would be the best candidate for supporting collaboration between the state, society, and private sector to address Russia's economic problems.

¶11. (U) However, these analysts pointed out that the GOR's focus on blue-collar workers in its anti-crisis measures had

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deprived the middle class of resources and opportunities to stimulate growth or reform. According to Tambovtsev, the main hope for middle class to play a transitional role in society lay in small business entrepreneurship. Unfortunately, the absence of secure property and contract rights, a biased judiciary, and administrative barriers impeded SME growth. Falling consumption was also hurting SME's, which tended to orient themselves toward household consumers. Without the resources and institutional reforms necessary to improve their productivity, middle class entrepreneurs were unlikely to serve as a strong countermeasure to current economic trends.

COMMENT

¶12. (C) While not dead, the Russian middle class does not show signs of rapid growth in the near term, nor does it seem likely to be the engine of democratic change in Russia. Better equipped to deal with the downturn than the working classes but politically inert, the middle class poses little threat to political and social stability. Moreover, despite the administration's emphasis on preparing for post-crisis development through innovation and small/medium businesses, the most likely candidate to help the government achieve those aims -- the middle class -- has largely been ignored by the state. We expect this process to continue: budget constraints will leave minimal resources for cultivating the human capital of the middle class. End Comment.
BEYRLE